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MAR 5 1985
ALEXANDER L. STEVAS,
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No. 84-885

IN THE

Supreme Court of the United States

OCTOBER TERM, 1984

NORFOLK AND WESTERN RAILWAY COMPANY,
CHESSIE SYSTEM RAILROADS, and
SEABOARD SYSTEM RAILROAD, INC.,
Petitioners,

v.

COAL EXPORTERS ASSOCIATION OF THE
UNITED STATES, INC., *et al.*,
Respondents.

On Petition for Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit

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REPLY BRIEF FOR PETITIONERS NORFOLK AND WESTERN RAILWAY COMPANY, CHESSIE SYSTEM RAILROADS AND SEABOARD SYSTEM RAILROAD, INC. IN SUPPORT

DONALD M. TOLMIE
ROLAND W. DONNEM
RICHARD B. ALLEN
EMRIED D. COLE, JR.
Of Counsel

R. EDEN MARTIN *
BENJAMIN W. HEINEMAN, JR.
G. PAUL MOATES
VINCENT F. PRADA
SIDLEY & AUSTIN
1722 Eye Street, N.W.
Washington, D.C. 20006
(202) 429-4000
Attorneys for Petitioners Norfolk and Western Railway Company, Chessie System Railroads and Seaboard System Railroad, Inc.

* Counsel of Record

March 5, 1985

WILSON - EPES PRINTING CO., INC. - 789-0096 - WASHINGTON, D.C. 20001

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Petitioners Norfolk and Western Railway Company, Chessie System Railroads and Seaboard System Railroad, Inc. submit this reply to the briefs in opposition filed by Respondents Coal Exporters Association of the United States, Inc. and National Coal Association ("CEA/NCA"), and by Eastern Coal Transportation Conference and Coastal States Energy Company ("ECTC").

(1) This case presents a substantial federal question—indeed a question of extraordinary significance—because

the Court of Appeals rejected, as a matter of law, the fundamental premise of railroad deregulation in particular and economic deregulation in general. Respondents argue that the Court of Appeals followed the intent of Congress in construing the exemption provision of the Staggers Act, the landmark railroad deregulation statute. 49 U.S.C. § 10505. *See* CEA/NCA Brief at 16-19; ECTC Brief at 14-17. This is plainly—and profoundly—wrong. This Court has not yet construed the Staggers Act and it should do so now to give effect to the deregulatory intent of Congress.

The fundamental premise underlying the Staggers Act and its exemption provision is that the *structure of the market* for surface freight transportation has changed. In 1887, when the Interstate Commerce Act was enacted, railroads were natural monopolies and held excessive market power because they faced no effective competition from other modes of transportation. Congress concluded that detailed, *prospective* rate regulation by the Interstate Commerce Commission (the "Commission") was necessary to protect shippers, consumers and other affected parties.[1]

In 1976, with the passage of the Railroad Revitalization and Regulatory Reform Act, Pub. L. No. 94-210, 90 Stat. 31 (1976), and in 1980, with the passage of the Staggers Rail Act, Pub. L. No. 96-448, 94 Stat. 1895 (1980), Congress found that the market structure for surface freight transportation had shifted dramatically and to the detriment of the railroads.[2] Rather than relying on the Com-

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[1] *See, e.g.*, T. Moore, "Deregulating Surface Freight Transportation," in *Promoting Competition in Regulated Markets* 77 (A. Phillips ed. 1975); S. Rep. No. 499, 94th Cong., 1st Sess. 10-11 (1975).

[2] In its legislative findings incorporated in the Staggers Act, Congress determined that although the enactment of the Interstate Commerce Act in 1887 had been necessary to prevent abuse of monopoly power by railroads, "today, *most* transportation within the United States [including rail transportation] is competitive,"

mission's elaborate, prospective rate regulation to protect the public interest, Congress sought "to allow, to the maximum extent possible, competition and the demand for services to establish reasonable rates for transportation by rail" and to "minimize the need for Federal regulatory control over the rail transportation system." 49 U.S.C. §§ 10101a(1), 10101a(2).

In the words of Representative Staggers, the 1980 Act, and the exemption provision which it amended, embodied a "totally new approach to the railroad industry" in which "competitive factors [would] be of paramount importance." 126 Cong. Rec. 28431 (1980). Congress clearly wanted the Commission to use its exemption authority aggressively to eliminate the elaborate agency line-drawing as to the "reasonableness" of rates which characterized the previous regime of prospective rate regulation. As stated in the Staggers Act Conference Report,

> The policy underlying this [exemption] provision is that while Congress has been able to identify broad areas of Commerce where reduced regulation is clearly warranted, the Commission is more capable through the administrative process of examining *specific regulatory provisions and practices not yet addressed by Congress* to determine where they can be deregulated consistent with the policies of this Act. H.R. Conf. Rep. No. 1430, 96th Cong., 2d Sess. 105 (1980) (emphasis supplied).

Moreover, the conferees anticipated that the Commission would

> eventually reduce its exercise of authority to instances where regulation is [(a)] necessary to protect against *abuses of market power* [and (b)]

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and that existing federal regulations affecting railroads "have become unnecessary and inefficient." Pub. L. No. 96-448, § 2, 94 Stat. 1896 (1980) (emphasis supplied) (reprinted in Historical Notes following 49 U.S.C.A. § 10101a).

> where other federal remedies are inadequate for this purpose. *Id.* (emphasis supplied).

With respect to such remedies, the conferees stated

> Particularly, the conferees expect that *as many as possible* of the Commission's restrictions on changes in prices and services by rail carriers will be removed *and that the Commission will adopt a policy of reviewing carrier actions after the fact to correct abuses of market power. Id.* (emphasis supplied).

When the Commission found such abuses, it had the power to revoke the exemption immediately, without notice and comment procedures. 49 U.S.C. § 10505(d); H.R. Conf. Rep. No. 1430, *supra*, at 104.

In sum, where the market characteristics for a particular rail service warrant it, the exemption provision authorizes the Commission to shift from a comprehensive regime of prospective rate regulation to deregulated arrangements which can be policed *after the fact* by the Commission on a case-by-case basis. Even where the affected carriers possess market power and there is an absence of "effective competition," Congress still declared it appropriate for the Commission to grant an exemption for a particular rail service so long as continued regulation is not necessary either to carry out the national rail transportation policy found in 49 U.S.C. § 10101a, or to protect shippers from "the abuse of market power," 49 U.S.C. § 10505(a).[3]

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[3] CEA/NCA thus completely misconstrue the exemption provision when they assert that a finding of "effective competition" or lack of market power is a necesssary prerequisite to an exemption from regulation. CEA/NCA Brief at 5, 23. As the Conference Report explicitly states, and as the Court of Appeals below conceded (App. 28a), the statute "permits exemptions wherever regulation is not needed to prevent abuses of market power, *regardless of the presence of effective competition.*" H.R. Conf. Rep. No. 1430, *supra*, at 105 (emphasis supplied).

In this case, the Commission clearly complied with the express requirements of the exemption provision, as well as the intent of Congress. It first found that seven of the fifteen elements of national rail transportation policy were advanced by an exemption for export coal transportation and that continued regulation was not necessary to implement the other eight policies. (App. 73a-88a). More importantly, it also found that the continued regulation of export coal was *not* needed to protect shippers prospectively from abuses of market power primarily because of the *characteristics of the market*, which was shaped by the international forces governing the export of U.S. coal and also by geographic, intermodal and intramodal competition within the United States. (App. 52a, 56a, 63a-64a, 84a-85a).

As a result, in its crucial finding, the Commission found that carriers and shippers have "relatively equal bargaining power" and that competition and pressures of supply and demand "will establish reasonable and rational rates for this traffic." (App. 74a-75a). Given this relatively equal bargaining power between carriers and shippers, prospective line drawing by the Commission as to reasonable rates for rail shipments of coal intended for export was no longer necessary. Accordingly, the Commission concluded that it was pointless to impose the economic burden of rate regulation on export coal traffic. After the fact review of any individual claims of abuse would adequately protect shippers. (App. 87a).

The Court of Appeals *accepted*, as a matter of fact, the Commission's crucial finding that the market for export coal transportation is characterized by relatively equal bargaining power between carriers and shippers. Nonetheless, it held that, as a *matter of law*, the Commission could not base an exemption on an analysis of market characteristics alone. Whereas the Commission found that the relatively equal bargaining power of the present export coal market structure would presumptively

yield reasonable rates in the future and any individual abuses could be remedied after the fact, the Court of Appeals demanded that the Commission go further and establish a clear nexus between existing market structure and a detailed prospective definition and prediction of "reasonable rates" which shippers would pay in the future. (App. 47a).[4] Only when the Commission had defined prospective "reasonable" rates with specificity and demonstrated in advance that such rates would result from present market structure could the Commission grant an exemption under the holding of the Court of Appeals. (App. 47a). Remarkably, the court never even discussed the Commission's authority to revoke the exemption after the fact in any individual instances when an abuse was shown, although the Commission had relied on this authority in concluding that continued regulation was unnecessary. (App. 87a).

In short, by refusing to allow an exemption based on an analysis of market characteristics alone, the Court of Appeals now requires the Commission *before* granting any exemption to engage in precisely the elaborate, prospective regulatory line-drawing as to "rate reasonableness" that the exemption provision had expressly been enacted to eliminate. Accordingly, this holding presents a substantial federal question because, if allowed to stand, it will vitiate "an important cornerstone" provision of the Staggers Act, a law which marked an historic change in the regulatory role of the Commission. H.R. Rep. No. 1035, 96th Cong., 2d Sess. 60 (1980).

(2) Respondents' attempts to downplay or excuse the errors in the Court of Appeals' decision are seriously

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[4] Respondents deny that the Court of Appeals' decision can be read to impose on the Commission a duty to make detailed predictive findings concerning the reasonableness of specific rates under an exemption. CEA/NCA Brief at 15; ECTC Brief at 18. Respondents' interpretation finds no support at all in the court's opinion (*see* App. 44a-47a), as recognized by the Solicitor General in his brief in this case. *See* Brief for United States at 12, 23-24.

flawed for several related reasons. First, and most important, Respondents completely ignore the Commission's critical finding that railroads and shippers of export coal have "relatively equal bargaining power" (App. 74a)—a finding that, like the Commission's other factual findings, the Court of Appeals declined to disturb. (App. 27a, 45a).[5] This finding, based on the extensive evidence of competitive restraints on railroad pricing actions, was the essential predicate for the Commission's ultimate conclusion that, when the exemption was in effect, the railroads would not be able to abuse any market power they might have, and that "market competition and natural forces of supply and demand, without interference from this regulatory agency, will establish reasonable and rational rates for this traffic." (App. 74a-75a). Respondents' opposition thus proceeds from a flatly incorrect view of the Commission's factual foundation for its ruling, a foundation left undisturbed by the Court of Appeals.

Ignoring the Commission's finding of relatively equal bargaining power between railroads and shippers, Respondents repeat an error committed by the court below, and assert that the Commission found that railroads would in fact possess significant market power, and that it had ruled that an exemption would be permissible even if the railroads could exercise such market power by appropriating virtually *all* of the economic rents and leaving shippers just enough revenues to cover their costs and remain in business. CEA/NCA Brief at 8-9, 14-15; ECTC Brief at 9-10, 13. *See* App. 37a. But such an interpretation is flatly erroneous. The Commission *never* found that the railroads would in fact enjoy substantial market power, or that they would or could appro-

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[5] Given the Court of Appeals' acceptance of all of the Commission's factual findings, Respondents' repeated citations to evidence that the Commission explicitly rejected, and their references to Chairman Taylor's dissenting remarks, have no legal significance in this case.

priate virtually all or even a substantial share of any available economic rents. Indeed, the Commission believed that it would be a "rare instance" in which railroads would have significant bargaining leverage over particular shippers. (App. 85a). Nor did the Commission adopt a legal standard that allows an exemption so long as total coal exports do not fall and shippers receive only a "bare minimum" of the rents. (App. 38a).[6] Rather, the Commission concluded that, in view of the existing competitive characteristics of export coal transportation, and the relatively equal bargaining power of the market participants, an exemption could be expected to result in "reasonable" rates and a fair allocation of the economic rents. Thus, Respondents, like the Court of Appeals, have grossly mischaracterized the thrust of the Commission's decision, with the result that they ignore the central finding of relatively equal bargaining power and competitive market structure.

(3) Respondents have also ignored the pertinent legislative intent and history of the Commission's exemption authority. In adopting the exemption provision in 1976 and substantially broadening its scope in 1980, Congress made clear that the provision established a strong presumption in favor of deregulation. This presumption is reflected in the command that the Commission remove "*as many as possible*" of the statutory restrictions on ratemaking and other carrier practices, and that it review railroad practices under deregulation "after the fact" to correct any unanticipated abuses of market power by railroads. H.R. Conf. Rep. No. 1430, *supra*, at 105.

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[6] Like the Court of Appeals, Respondents' error derives from a misreading of the Commission's discussion of price discrimination. The purpose of that discussion was not to show that railroads do in fact have substantial market power. Rather, the limited purpose was to show that, even *if* some railroads might have some degree of market power, they would not "abuse" such power by increasing rates to the point where total export coal production would fall, or where shippers would be forced out of the market.

Respondents do not even acknowledge this dispositive legislative history. They argue, instead, that because Congress in enacting the Staggers Act retained certain regulatory provisions governing maximum rail rates for all commodities, including coal, those provisions are inviolate and beyond the Commission's exemption power unless the Commission, *before* granting an exemption, demonstrates in detail that those statutory standards of rate reasonableness will be fully satisfied under deregulation.[7] This view, accepted by the Court of Appeals, would render the exemption provision virtually meaningless, for the declared purpose of that provision was to authorize—indeed command—the Commission to *go beyond* those areas already deregulated by Congress. By reading the regulatory standards of rate reasonableness back into the exemption provision, Respondents and the Court of Appeals have reversed the presumption in favor of deregulation and have subverted Congress's intent to authorize exemptions from regulation on the basis of an assessment of market characteristics, with "after the fact" review to correct possible abuses.[8]

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[7] CEA/NCA, for example, baldly assert that the Commission is powerless to grant exemptions from those provisions of the statute that Congress in the Staggers Act decided to retain. CEA/NCA Brief at 19. That view, of course, would prevent the Commission from granting *any* exemptions. Similarly, ECTC complains that the Commission failed to observe the standards of rate reasonableness it has developed for domestic coal traffic, thus confirming its view that the exemption provision incorporates all pre-existing regulatory standards. ECTC Brief at 13.

[8] Respondents also question the significance of the decision below because the D.C. Circuit does not have exclusive jurisdiction over appeals from Commission exemption decisions. *See, e.g.*, CEA/NCA Brief at 23. This argument overlooks the crucial point, which is that because venue is always available in the D.C. Circuit in such cases, parties seeking to overturn future exemptions from regulation will naturally bring their petitions for review in the D.C. Circuit to obtain the benefit of that court's erroneous holding in the instant case.

CONCLUSION

For the foregoing reasons, the petition for a writ of certiorari to the Court of Appeals for the District of Columbia Circuit should be granted.

Respectfully submitted,

DONALD M. TOLMIE
ROLAND W. DONNEM
RICHARD B. ALLEN
EMRIED D. COLE, JR.
Of Counsel

R. EDEN MARTIN *
BENJAMIN W. HEINEMAN, JR.
G. PAUL MOATES
VINCENT F. PRADA
SIDLEY & AUSTIN
1722 Eye Street, N.W.
Washington, D.C. 20006
(202) 429-4000

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* Counsel of Record

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